

# MÉMOS BANQUE

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## N°03

# HOW TO SUCCESSFULLY FINANCE THE ENERGY TRANSITION



The Green supporting factor<sup>(1)</sup> :  
How to successfully finance  
the energy transition.  
Proposal by the French banking  
industry.



(1) Preferential prudential treatment for bank assets that support energy transition.

# THE CHALLENGES OF THE PARIS AGREEMENT

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📍 The Paris Agreement, approved at the COP 21 in November 2015, seeks to «hold the increase in the global average temperature to well below 2° C above pre-industrial (1880) levels, recognizing that this would significantly reduce the risks and impacts of climate change».

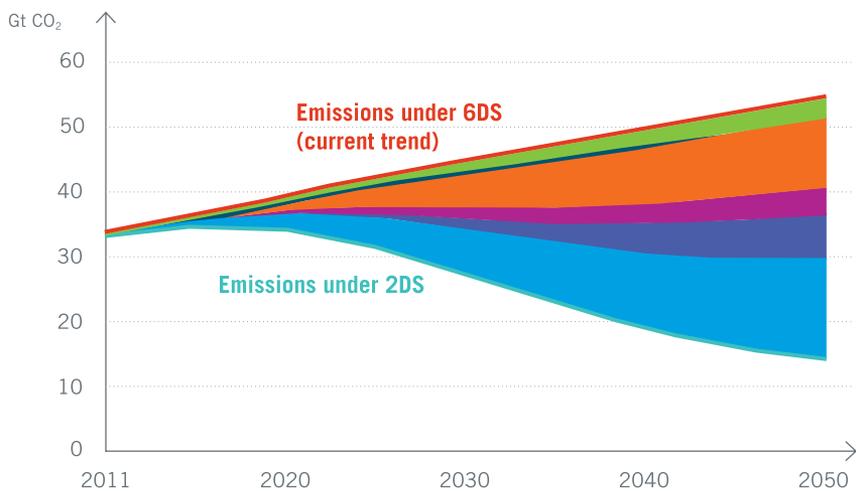
📍 According to the International Energy Agency's (IEA) 2015 World Energy Outlook report 2015<sup>(1)</sup> the aims of the agreement can only be met **if certain measures are put in place**, including measures to reduce emissions of CO<sub>2</sub> and other greenhouse gases. The IEA has identified these measures in its 2°C scenario (2DS)<sup>(2)</sup> which sets out the path that emissions need to follow if the 2°C target is to be met (see chart below).



(1) The report seeks to better understand the scale and nature of the challenges posed by energy transition over the next forty years: how best to improve energy security, energy efficiency and the reduction of greenhouse gas emissions, and how to guide innovation and R&D toward the most promising areas.

(2) A scenario that provides at least a 50% probability of limiting temperature rises to less than 2°C, through a near 60% reduction in global GHG emissions by 2050 compared to 2013; this still allows for a total of 1,000 billion tonnes of CO<sub>2</sub> to be emitted between 2013 and 2050.

## TRANSITION FROM CURRENT TREND TO 2° SCENARIO



- Nuclear **8%**
- Power generation efficiency improvements and migration to non-oil alternative fuels **1%**
- Renewable energies **30%**
- Migration to non-oil alternative fuels **10%**
- Carbon capture and storage **13%**
- Energy saving **38%**

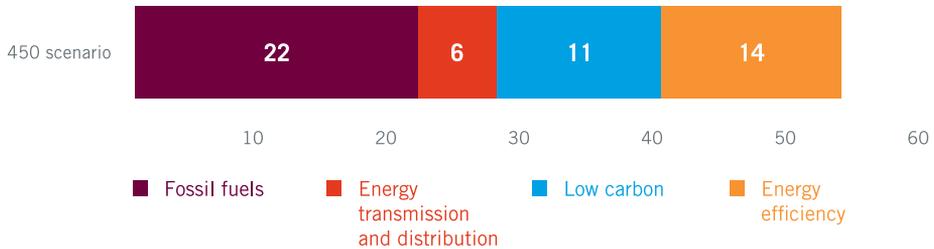
Source: International Energy Agency (IEA)

 Compliance with all these measures to reduce GHG emissions will demand major investment.

The IEA estimates the investment required over the next twenty years at US\$ 53,000 billion.

### TOTAL INVESTMENT IN THE 450 SCENARIO<sup>(1)</sup>, FROM 2014 TO 2035

In € billions (2012)



Source: International Energy Agency (IEA)



**60%**

**INVESTMENT  
IN NEW ENERGIES**

**53**

**TRILLION DOLLARS  
INVESTMENT OVER 20 YEARS**

**40%**

**INVESTMENT  
IN ENERGY SAVING**

(1) A "450" scenario that sets out changes in the global energy system that would reduce greenhouse gas emissions to a level limiting global warming to 2°C above pre-industrial temperatures.

# OUR PROPOSAL: THE GREEN SUPPORTING FACTOR

📍 The key challenge is to reduce the relative cost of investing in the energy transition, by cutting either equipment costs or financing costs.

📍 Industrialisation and rising volumes have had highly positive effects on the cost of equipment.

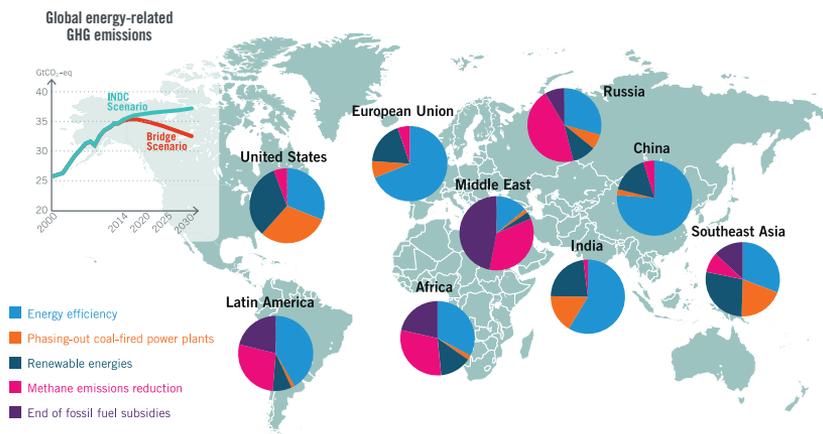
📍 Despite the low-interest rate environment and growing awareness of the low-risk nature of these assets, the cost of

financing the energy transition remains a major challenge.

📍 Therefore, to support and accelerate the financing of these assets in an economy where 70% of finance comes from banks, it is essential to recognize the beneficial nature of such assets for the energy transition and, ultimately, for the mitigation of systemic risk to the planet.

## REDUCTION IN GREENHOUSE GAS EMISSIONS BY MEASURE, IN A TRANSITION SCENARIO, COMPARED TO THE INDC SCENARIO<sup>(1)</sup>, 2030

Source: World Energy Outlook Special Report: Energy and Climate Change (2015).



(1) INDC: National submissions to the international negotiation process

# 1 HOW THE GREEN SUPPORTING FACTOR WORKS

 In this context, **the FBF wants to propose an «appropriate prudential approach» to financing and investment** in the energy transition (incentivising decarbonisation of bank balance sheets) to recognize the macro-prudential benefits of these assets in reducing the probability of these climatic risks.

From a regulatory perspective, this should mean lower capital requirements for financing and investing in these assets.

To achieve this we are asking for the introduction of a supporting factor applicable to capital requirements for exposure to assets that support the energy transition: **the «Green supporting factor»**.

This would work in a similar way to the already proven SME supporting factor<sup>(1)</sup>.

# 2 ELIGIBLE ASSETS BASED ON RECOGNIZED CERTIFICATIONS

 To identify which assets are eligible, we propose using rules laid down by widely recognized certifying bodies such as the French “Transition énergétique et écologique pour le climat” (TEEC) certificate or the terminology used by the **Climate Bond Initiative** or any other label with the same characteristics.

Assets benefiting from the Green supporting factor could include:

- **financing or investment granted to counterparties whose business relates to energy transition<sup>(2)</sup>**. The bank in question would rely on an external certification body to confirm the counterparty’s eligibility.
- **other financing or investment whose purpose relates to energy transition<sup>(2)</sup>**.

(1) Article 501 of European Parliament and Council Regulation 575/2013 (the CRR) envisages the application of a 0.7619 factor to capital requirements for credit risks on exposures to SMEs.

(2) For instance, the types of investment described in Appendix I to the TEEC certification specifications.

# 3 ALL PARTICIPANTS IN THE ECONOMY WOULD BE ELIGIBLE

📍 To ensure the successful financing of the energy transition, the counterparties eligible for the «Green supporting factor» should include **any and all participants in the economy, whether financed through retail banking networks or corporate and investment banking**: individuals, SMEs, companies, banks and sovereign bodies.

For instance, eligibility for the Green supporting factor would cover:

- **financing for individuals** to buy an electric car or pay for energy efficiency improvements,
- **financing for an SME** to construct a green building,
- **financing for companies** that build or operate solar, wind or energy storage infrastructure,
- investment in green bonds issued by **sovereign issuers** such as the French government's Obligation Souveraine Carbone (OSC).





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